

Detecting Fraud and Illegal Acts

AICPA Statement of Auditing Standards (SAS) No. 99, *Consideration of Fraud in a Financial Statement Audit* and Statement on Auditing Standards No. 54, *Illegal Acts by Clients* provide guidance on the auditor's responsibility to detect fraud and illegal acts.

The *Audit Manual* and the Contract to Audit Accounts require the auditor to immediately report in writing to the Comptroller of the Treasury any evidence of fraud, such as defalcation, misappropriation, misfeasance, malfeasance, embezzlement, or other illegal acts.

The Department of Audit conducts special-purpose examinations of governmental entities previously audited by certified public accounting firms and conducts working paper reviews of government audits performed by certified public accounting firms. These examinations and reviews often result in the discovery of fraud that was not detected by the previously performed audits. The Comptroller of the Treasury has summarized the areas where undetected fraud has occurred most often and accordingly determined them to be high-risk areas. Auditors should document that these high-risk areas were considered during the fraud risk assessment process required by SAS No. 99. The Department of Audit will determine if these areas were considered when it conducts working paper reviews of governmental audits performed by public accounting firms. These high-risk areas are listed as follows:

1. Cash Collections

Suggested Procedures - SAS No. 99 requires an audit response to fraud risks that the auditor identifies as representing a risk of material misstatement of the financial statements unless those risks are mitigated by the government's antifraud programs and internal controls. If the auditor needs to extend audit procedures in response to a risk of material misstatement due to fraud involving cash collections, the Department of Audit has found certain audit procedures to be highly effective in detecting schemes involving misappropriation of cash. The procedures are suggested but not required. If the following procedures are already being performed, consider expanding their extent.

- Review the makeup of deposits and determine that the cash and check ratio agrees with source documents (cash and checks collected).
- Review deposit slips and determine that receipts itemized on the deposit slips are recorded in the receipt books.

- Determine that deposits are being made intact and at least daily. (State law requires that deposits be made within three days of receipt).
- Perform surprise cash counts.
- Send third-party confirmations for significant revenues received in the mail.

2. Unrecorded bank accounts

3. Vending machine revenues

4. Unauthorized or fraudulent cash disbursements

5. Purchasing

6. Travel expenses and reimbursements

7. Credit cards and procurement cards

8. Use of government equipment, labor, materials and supplies

9. Use of government owned vehicles

10. Gasoline usage